IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 06.02.2007

CORAM

THE HON'BLE MR.JUSTICE P.D.DINAKARAN
AND
THE HON'BLE MRS.JUSTICE CHITRA VENKATARAMAN

T.C.(R)Nos.175 and 176 of 2003

Commissioner of Income Tax
Chennai. .. Applicant

Vs.

M/s. Tractors and Farms
Equipments Ltd.,
Chennai 34. .. Respondent

Reference under Section 256(1) of the Income Tax Act, 1961 at the instance of the revenue arising out of the order of the Income Tax Appellate Tribunal, Madras 'C' Bench dated 14.01.1998 in ITA Nos.4500 & 4501/Mds/1989 for the assessment years 1982-83 and 1985-1986. against the order of the officer of the Commissioner of ;Income _Tax (Appeals) V madras -34 dated 13.9.89 in IT Appeal. No. 70 and 69/89-90 against the proceedings of the Deputy Commissioner of Income tax Special Range 1 Madras 34 in G.I. No. I-T/82-83/47-004-CT-7442 and GI. No.I-T/85-86/47-004CT-7442 dated 13.4.89.

For applicant : Mrs. Pushya Sitaraman, Sr.SC.for IT

For Respondent : Mr. R. Venkatnarayanan for
M/s. Subbaraya Aiyar

J U D G M E N T

(Delivered by P.D. DINAKARAN, J.)

At the instance of the Revenue, the Income-tax Appellate Tribunal has stated a case and referred the following question of law, which is common in both tax cases:

> "Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the interest paid under deferred payment scheme under which certain assets acquired is capital in nature and investment allowance is allowable on the same?"

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2.1. The assessment years with which we are concerned are 1982-83 and 1985-86. The assessee is a company. The assessee claimed investment allowance on the interest paid under the deferred payment scheme through which certain assets were acquired, which was negatived by the assessing officer.

2.2. The Commissioner of Income-tax (Appeals) allowed investment allowance holding that the interest accrued under the deferred payment scheme is capital expenditure. The Appellate Tribunal upheld the order of the Commissioner of Income-tax (Appeals).

2.3. While giving effect to the said order, the assessing officer found that the requisite reserve had not been created, and denied the benefit obtained by the assessee in terms of the above order of the Appellate Tribunal.

2.4. On appeal, the Commissioner of Income-tax (Appeals) accepted the contention of the assessee that the assessee should be afforded an opportunity to make good the shortfall in the creation of reserve, and remitted the matter to the assessing officer. On further appeal, the Appellate Tribunal confirmed the same.

2.5. At the instance of the Revenue, the Appellate Tribunal has stated a case and referred the above mentioned question of law.

3. Undisputedly, the assessee purchased capital assets on deferred payment basis from the manufacturer availing the facility extended by I.D.B.I. Bank called, "I.D.B.I. Bills Rediscounting Scheme". Under the scheme, the purchaser utilised the machinery acquired from the date of purchase and the manufacturer got the value of the machinery within a few days of the delivery of the machinery. The payment of price in instalments was worked out and each instalment was computed by adding interest. While the instalments of the price were equal, the interest component would be higher with the passage of time. The manufacturer was required to present the bill at the bank of the purchaser for discounting within two months and the bank, in turn, would present the bill for rediscounting with I.D.B.I.

4. According to the assessee, the total amount of the instalments including the interest is the actual cost of the assets purchased within the meaning of section 43(1) of the Income-tax Act, 1961 (in short "the Act"), the relevant portion of which reads as under:

> "43(1). 'actual cost' means the actual cost of the assets to the assessee, reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority."

5. On the other hand, the Revenue contends that the interest paid on capital borrowed after commencement of business cannot be capitalised. In this connection, it is relevant to refer the Explanation-8 to section 43(1) as follows:

> "Explanation 8.--For the removal of doubts, it is hereby declared that where any amount is paid or is payable as interest

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in connection with the acquisition of an asset, so much of such amount as is relatable to any period after such asset is first put to use shall not be included, and shall be deemed never to have been included, in the actual cost of such asset".

6. The Appellate Tribunal, however, on the facts of the case held that the amount paid by the assessee as interest is not actually an 'interest amount' paid on capital directly borrowed from the financial institution for the purpose of purchasing the capital asset and the instalments paid constituted only the actual price of the asset since the invoice shows the total price including the financial charges. According to the Tribunal, the enhanced price due to the facility given by the I.D.B.I. Scheme for deferred payment is quite distinct from either interest paid on capital borrowed or interest paid on unpaid price and hence, Explanation 8 to section 43(1) of the Act has nothing to do with the enhanced price of goods sold under the I.D.B.I. Scheme.

7. In our view, Explanation 8 to section 43(1) of the Act, inserted with effect from April 1, 1974, should not be construed in the way as adopted by the Appellate Tribunal. A reading of the Explanation 8 to section 43(1) of the Act shows that it was added with the object of removing doubts with regard to the includibility of interest relatable to any period after the asset has first been put to use, in the computation of its actual cost. By this Explanation, it has been declared by Parliament that "where any amount is paid or is payable as interest" in connection with the acquisition of an asset "so much of such amount as is relatable to any period after such asset is first put to use shall not be included and shall be deemed never to have been included," in the actual cost of such assets. The Parliament, in the above Explanation, has taken full care to couch the Explanation in the widest possible terms to avoid any further controversy in regard to the very same issue on the basis of the manner of payment of interest or time of payment thereof. This has been done by the use of the expression "where any amount is paid or is payable as interest". It will not be correct to say that the legal position in regard to includibility of interest on deferred payment in the computation of the actual cost of an asset did not undergo any change as a result of the insertion of Explanation 8 with retrospective effect and the specific declaration by Parliament made therein that the part of the interest mentioned therein would not be includible in the actual cost. The very purpose of this amendment was to clarify the position in this regard and to set at rest the controversy that had arisen, vide CIT v. Rajaram Bandekar (202 ITR 514 – Bombay High Court).

8. Applying the ratio laid down by the Bombay High Court in CIT v. Rajaram Bandekar, cited supra, this Court in CIT v. India Pistons Ltd. (242 ITR 672), held as follows:

> "In the instant case, depreciation has been claimed on interest payable on a deferred payment scheme which is identical to the facts involved in the case decided by the Bombay High Court reported in CIT v. Rajaram Bandekar [1993] 202 ITR 514. We concur with the view taken by the Bombay High Court.
>
> We hold that the amount of interest could not be included in the actual cost for the purpose of depreciation and development rebate applying Explanation 8 to section 43

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(1) of the Income-tax Act, 1961. The view taken by the Tribunal is not justified."

9. The above view has also been followed by this Court in CIT v. L.G. Balakrishnan and Brothers Ltd. (247 ITR 131).

10. This Court in C.I.T. v. Textool Co. Ltd. (263 ITR 523) also held that in view of Explanation 8 to section 43(1) any amount paid as interest in connection with the acquisition of an asset shall not be included and shall never be deemed to have been included as part of the actual cost of the asset.

11. In this view of the matter, we hold that the amount of interest payable on deferred payment scheme could not be included in the actual cost for the purpose of investment allowance applying Explanation 8 to section 43(1) of the Act, and the Appellate Tribunal is not correct in holding that the interest paid under deferred payment scheme is capital in nature and investment allowance is allowable on the same.

Accordingly, the common question of law referred to us is answered in the negative, in favour of the Revenue and against the assessee. No costs.

Sd/
Asst. Registrar

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Sub Asst.Registrar

To

1.The Assistant Registrar,
Income Tax Appellate Tribunal
Madras.
2.The Secretary, Central Board
of Direct Taxes, New Delhi.

3.The Commissioner of Income-
Tax (Appeals-V), Madras.

4.The Deputy Commissioner
of Income-tax, Special Range I,
Madras.
5. The ITAT C Bench, Madra.s

+ One cc to Mr. R. Venkataraman Advocate SR 7084
+ One cc to Mrs. Pusya Sitaraman Advocate SR 7521
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